DAVID R. KERN
ASSET MANAGEMENT
Dynamic Asset Allocation Strategies
www.davidrkern.com

4th Quarter 2007 Newsletter

The Big Picture

As 2007 drew to a close it became increasingly clear that the U.S. economy was slowing down. The broad stock market indexes went down in the last two months of the year. For the 12 months ending December 31st, the S&P 500 Index was up 3.53%, the Dow Jones Industrial Average up 6.43%, and other major indexes around the world generally posting better gains. Some of the International markets found in the emerging countries had gains in excess of 20% as investors moved money to areas with potentially higher growth. Some of the fear of investing in "third world countries" has receded over the last couple of years as it becomes clear that natural resources like oil and basic materials owned by these countries will continue to become more valuable.

Amid a backdrop of geopolitical tension, a weakening dollar, and increasing demand, crude oil has continued to surge and for a brief moment hit $100.00 per barrel. Global demand for oil has altered the wealth and influence of nations and industries around the world, primarily enriching the Middle East, Russia, and Venezuela. For the year, oil prices are up 50% with the U.S. and China as the largest consumers of oil.

To counter the slowing economy, the Federal Reserve lowered interest rates for a third time in December in the hopes of averting a recession. The last time the Fed lowered rates for three consecutive meetings was in 2001, six years ago, in an attempt to bring us out of the financial bear market that started in the spring of 2000 and ran for three years.

The optimistic case can be made that the world has changed over the last few years, with economies outside the United States providing diversification and growth to help offset some of the declines in other parts of the world. While world economic growth may slow in 2008, at some point during the year a great buying opportunity will emerge for beaten down equities in certain industries, and sectors.

Another positive aspect of slower growth may be in the moderation of the demand for oil, which may allow the price to ease and reduce inflation.

Gold is a volatile commodity with wide ranging price swings, but the price of an ounce of gold is approaching $900.00 for the first time. The high price of gold and oil combined with the slowing economy brings back memories of the 1970s when America suffered a period called "Stagflation". This was characterized by stagnate economic growth and surging inflation. Back in the 1970s when oil prices skyrocketed, the Government decided to freeze the price of gas, resulting in long lines at the gas pump. Free market supply and demand were out of whack because oil companies couldn't provide enough gas to meet demand. If the economy does start to slow, it may cool demand around the world, and help bring the price of some commodities like gold and oil back down to earth.

A Good Year For Active Management

Our actively managed programs are providing both risk management, and positive returns in the current difficult stock market environment. Our duel objectives are to preserve principal in down markets, and participate in gains when markets are rising. Our quantitative programs for portfolio management means we've done our homework in calculating risk in market cycles. The value added by our risk management is often best understood when, in contrast to our management, passive "buy and hold" allocation models are losing money in the stock markets.

Please contact David R. Kern Asset Management if there are any changes in your financial situation or investment objectives, or if you wish to impose, add or modify any reasonable restrictions to the management of your account. Our current disclosure statement is set forth on Part II of Form ADV and is available for your review upon request.

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